CO-OPERATIVE CENTRAL BANK LIMITED

v.

G VISVANATHAN GOVINDASAMY & ORS

HIGH COURT MALAYA, PENANG
RK NATHAN J
[CIVIL SUIT NO: 23-315-1988]
25 MARCH 2002

CONTRACT: *Guarantee - Demand for payment - Letter of guarantee - Validity - Whether obtained by fraud and concealment of facts - Joint guarantee - Contracts Act 1950, s. 97 - Failure to produce letter from co-guarantor - Whether guarantee rendered invalid*

EVIDENCE: *Adverse inference - Whether presumption to be raised - Non-production of material witness - Evidence Act 1950, s. 114(g)*

The plaintiff executed a loan agreement with one Mutuerulan (the principal borrower) and the defendants signed a letter of guarantee as guarantors for the said loan. When the principal borrower defaulted on the loan payments, the plaintiff sought to claim the sum together with interest, from the defendants. This dispute arose when the defendants refused to pay the plaintiff the sum in question. They contended that the letter of guarantee was not valid in law and was unenforceable as it had been fraudulently obtained by the plaintiff and the principal borrower. The 4th defendant submitted the defendants agreed to sign the guarantee letter because the plaintiff's bank manager had assured him of the principal borrower's financial credibility in that his nett income was RM80,000 per month and he owned a ship worth US1.2 million.

Held:

[1] The plaintiff's case was bare and devoid of any proof of any salient facts at the close of its case. (p 348 b)

[2] Despite the fact that the 4th defendant had alleged that the plaintiff's bank manager had fraudulently assured them of the principal borrower's credibility, the plaintiff did not call the said manager to testify so as to rebut the 4th defendant's evidence. Under s. 114(g) of the Evidence Act 1950, an adverse inference was drawn against the company in that the testimony of the said manager would have been unfavourable to the plaintiff's case had he testified. (pp 348 h & 349 a)

[3] It was in evidence that the loan had been disbursed before the 4th defendant signed the letter of guarantee and charged his property as collateral. (p 349 b-c)

[4] The plaintiff did not plead any agreement nor any breaches thereof in its pleadings. Further, there was no proper demand made as the notice of demand was undated and there was no proof that the defendants had been served with the proper demand. (p 349 d)

[5] The plaintiff did not tender the documents which the principal borrower should have furnished before obtaining the loan, such as his tax returns, bank statements for six months and a further guarantee from the local directors of Far East Shipping SA, the purported owners of the ship which was connected to the principal borrower. (p 349 h)

[5a] In absence of a guarantee from the said directors, s. 97 of the Contracts Act 1950 renders the guarantee invalid. Surely, the present defendants were entitled to seek contribution from the said directors of the shipping company. (pp 350 b-c & 351 a)

[Claim dismissed with costs.]

Case(s) referred to:
Len Min Kong v. United Malayan Banking Corp Bhd & Anor [1998] 2 CLJ 879 ***(foll)***

Legislation referred to:
Contracts Act 1950, s. 97
Evidence Act 1950, s. 114(g)

For the plaintiff - S Anthonysamy; M/s Aziz, Anthony & Co
For the defendants - Mohd Hussain Ibrahim (M Kanesan); M/s Hussain Ibrahim & Co

Reported by M Maheswaran

JUDGMENT

RK Nathan J:

Facts

The plaintiff, a co-operative society registered under the co-operative ordinance 1948, by way of an agreement in writing, agreed to lend to one Mutuerulan s/o Irulandi on or about 31 December 1982 a sum of RM600,000 (the loan) which the said Mutuerulan s/o Irulkandi agreed to pay by monthly instalments over a period of 60 months at an interest rate of 15% per annum at yearly rests which was subject to default in interest at 11/3 times the interest rate at monthly rest on the overdue instalments within the agreed period of 60 months. By a letter of guarantee dated 27 January 1983 all the defendants guaranteed to repay the said loan together with the interest in the event of default or non-payment of the instalment by the said Mutuerulan s/o Irulandi to the

plaintiff. Neither the said Mutuerulan s/o Irulandi nor the defendants have repaid the accrued sum of RM1,789,860.81 as at 31 January 1988 in spite of a notice of demand.

The Plaintiff's Claim

The plaintiff therefore prayed for:

1) Payment of the said sum of $1,789,860.81 as at 31 July 1988.

2) Interest at the rate of 14.50% per annum at yearly rests from 1 August 1988 to date of final settlement and further interest at 19.33% per annum at monthly rests and the instalment in arrears from 1 August 1988 to date of full settlement.

3) Interest at the rate of 14.50% per annum at yearly rest from the date of judgment to the date of full settlement and interest at 19.33% at monthly rests on the overdue instalment from the date of judgment until date of satisfaction or realisation.

4) Costs.

5) Such further or other relief as the court may deem fit.

The Defence

The defence was that the letter of guarantee was not valid in law and was unenforceable as it was obtained by fraud, concealment of material facts, misrepresentation and deceit, practised by the plaintiff and the principal borrower on the defendants.

Findings Of The Court

On the day fixed for hearing of this very old and outstanding case, Mr S Anthonysamy for the plaintiff, called as his first and only witness one Foo Yu Kam @ Cheong Poh Lim, the credit officer of Ex-CCB Assets and Liabilities Management attached to the Phileo Allied Bank (Malaysia) Bhd. Having introduced herself as such, she then went on record as saying that she was actually an officer of the Malayan Banking. During her examination-in-chief Mr Anthonysamy attempted to admit a letter purportedly written by the defendants admitting the loan. This letter was hotly challenged by the defendants. Caught in this dilemma, counsel pleaded with the court to mark the letter as ID and that he would prove the same subsequently. The court then marked the said letter as ID1. Under cross-examination the witness admitted taking over the files relating to this matter only in 1995 and she very frankly conceded that she had no knowledge of any of the documents prior to taking over, in 1995. She also admitted readily that she did not know if the principal borrower had complied with the terms and conditions contained

in the letter of offer. After this witness had testified, counsel for the plaintiff asked for an adjournment to get more relevant witnesses. Although I had put this case through case management, yet at the behest of counsel I granted an adjournment. When court resumed on the next occasion, I was most surprised when Mr Anthonysamy informed that he was closing his case.

Now even at this stage if the defendants had submitted no case to answer I would have readily accepted the said submission. The plaintiff's case was bare and devoid of any proof of any salient facts at the close of its case.

The defendants decided to allow the 4th defendant to speak for all of them and to be bound by his evidence. However, I allowed the plaintiff's counsel the right to cross-examine any of the other defendants if he chose to do so. The 4th defendant testified that he was approached by the principal borrower, whom he knew as a customer of the United Asian Bank (UAB) when he was working there, to stand as his guarantor. Before he actually did so, he met up with the Penang Bank manager of the plaintiff, one Eu Eng Keat, who assured him that based on the working paper submitted to the plaintiff by the principal borrower, the nett income of the principal borrower was RM80,000 per month and that he also owned a ship worth US$1.2 million. He was also reassured of the principal borrower's credit worthiness when the bank manager told him that if the bank felt that the principal borrower was unable to repay the loan, the bank would never approve the loan. Because of these assurances he not only signed the guarantee, he persuaded the 1st, 2nd and 3rd defendants who are his siblings, to also sign the guarantee. Further, based on these assurances he testified that he not only signed the guarantee, he also charged his valuable property as collateral. The plaintiff had in any case foreclosed on the said property. Under cross-examination the 4th defendant admitted that in the foreclosure proceedings he had not raised the issue of fraud and concealment of material facts because he was not aware of all these facts which he only became privy to, when he started his own investigations after finding out that the loan was released even before he had signed the guarantee agreement. He had commenced his investigations only after the principal borrower had defaulted in his repayment.

It was put to the 4th defendant that the bank manager was never involved in persuading him to sign the guarantee. In any case the defendants and in particular the 4th defendant had specifically named this bank manager in the defence and pleaded fraud and concealment of material facts. In spite of putting to this witness that the bank manager was never involved, I was surprised when the plaintiff closed its case without calling the bank manager or without giving any reasonable explanation for his absence. Even if the plaintiff had closed its case, yet soon after the 4th defendant' s evidence, no application was made to call the bank manager to rebut the 4th defendant's

evidence. To my mind this is a clear case as any to invoke s. 114(g) of the Evidence Act 1950 and to draw an adverse inference against the plaintiff in that had the bank manager been called, his evidence would have been unfavourable to the plaintiff.

I was impressed with the evidence of the 4th defendant. He was forthright and candid. Whilst his counsel had successfully marked the letter of the defendants as ID1 he readily admitted to having sent the admission letter. But he said that the letter was sent soon after the demand was made. He was then unaware of the machinations of the bank manager and the principal borrower. What is of telling effect is that whilst the loan was disbursed on 31 December 1982, he only signed the guarantee on 27 January 1983 and charged his property as collateral on 1 September 1983 and he told the court that had he known that the loan was already disbursed he would not have signed the guarantee nor charged his property.

Another factor I ought to consider is that the plaintiff in its pleadings never pleaded any agreement nor any breaches thereof. Further there is no proper demand made because even the demand notice is undated and there is no proof that the defendants had been served with the proper demand notice. Under the terms of the guarantee it must be shown that demand has been made and in writing and signed by the official and posted to the address stated in the guarantee. However in para. 6 of the statement of claim the plaintiff had averred that on 3 September 1983 it had sent a notice of demand to all the defendants. This paragraph has been denied and yet the plaintiff had failed to tender this particular letter as having been sent by the plaintiff and received by the defendants. However, an undated notice has been included in the common agreed bundle of documents (CABD) which has been addressed to the principal borrower and to all the defendants. Whilst the 4th defendant's address for service as stated in the guarantee agreement is 161C Argyll Road, Penang, the undated notice was sent to the 4th defendant at 81-91 Jalan Sultan Yusof, Ipoh. Whilst the undated letter was addressed to the lst, 2nd and 3rd defendants at 161C Argyll Road, Penang the defendants had denied receipt of the said letter. In the circumstances it was incumbent upon the plaintiff to show proof of posting or receipt of the letter by the defendants. Unfortunately, the plaintiff failed to do so.

Another vital factor relied on by the defendants is that there was no evidence to show if the principal borrower had in fact fulfilled the terms and conditions before the loan was released to him. Amongst the many terms listed in the letter of offer were that the principal borrower was requested to furnish:

1) tax returns to substantiate his income.

2) Six months bank statement.

3) Further guarantee from the local directors of Far East Shipping SA which purportedly owned the ship.

None of these documents were tendered nor put into the CABD although raised in the defence.

In the absence of evidence that the local directors of Far East Shipping SA had also signed as guarantors I agree with the submission of Mr Kaneson for the defendants that s. 97 of the Contracts Act 1950 will assist the defence. The section reads as follows:

> Where a person gives a guarantee upon a contract that the creditor shall not act upon it until another person has joined in it as co-surety, the guarantee is not valid if that other person does not join.

In *Len Min Kong v. United Malayan Banking Corp Bhd & Anor* [1998] 2 CLJ 879 Gopal Sri Ram JCA in dealing with this section and having referred to numerous authorities distilled the following propositions after analysing the authorities. He sets them out at p. 901 of the judgment as follows:

> In our judgment, the following propositions may be culled from the authorities under discussion:
>
> (1) Section 97 of the Contracts Act 1950 embodies the rule invented by the Court of Chancery to relieve sureties from the burden of their liability which, but for the operation of the rule, would be strict at common law.
>
> (2) When interpreting s. 97, guidance may reasonably be sought from cases decided in other jurisdictions which, while recognising the existence of the rule, do not have any provision in their written law that is parallel to s. 97 of our Act or s. 144 of the Indian statute.
>
> (3) The phrase 'upon a contract' appearing in s. 97 does not confine the parties to the contract of guarantee itself but includes an arrangement between them, collateral to the main contract, whereby it is contemplated that more than one person should execute the guarantee. In other words, a guarantor who invokes the benefit of the section is not confined to the four corners of the contract of guarantee when seeking to establish the existence of the contract of which the section speaks. He is at liberty to adduce evidence *aliunde* to demonstrate that there existed an arrangement between the parties that made his liability under the guarantee depend upon the execution of the guarantee by another guarantor.

Having seen the letter of offer in this case I am of the view that the third proposition distilled by the Court of Appeal in *Len Min Kong (supra)* fits this case. Surely the present defendants are entitled to seek contribution from the local directors of the shipping company.

Having heard the evidence of the 4th defendant and which evidence I accept as unchallenged, I had no hesitation in dismissing the claim with costs.